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Report Highlights:

On September 21, 2011, the Russian Government (GOR) approved a Forecast of Socioeconomic Development for 2012 and the planning period of 2013-2014. The report includes an overview of the Ministry of Economic Development's macroeconomic assumptions, a summary of tax, customs and tariff, and budget policy measures planned for agriculture, as well as sector-specific production forecasts on grain, sugar, oilseeds, meat, poultry, dairy, fishery, forestry, and food retail/catering.

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Summary

On September 21, the Russian Government approved a Forecast of Socioeconomic Development for 2012 and the planning period of 2013-2014 (hereinafter – the Forecast), prepared by the Ministry of Economic Development (MED). MED develops such forecasts every year as part of the Russian government's process of developing its three-year federal budgets, thus Russia's budget is based on the MED forecast data. MED's forecasts are subject to regular revisions later on; in fact, on November 29, 2011, MED Minister Nabiullina announced that agricultural production in Russia is expected to increase by 17% in 2011, above the 13.7% currently projected by the Forecast. Nevertheless, the document offers a comprehensive outlook for Russia's agricultural development in 2012-2014 as seen by the government of the Russian Federation. The report includes an overview of MED's macroeconomic assumptions, a summary of tax, customs and tariff, and budget policy measures planned for agriculture, as well as sector-specific forecasts on grain, sugar, oilseeds, meat, poultry, dairy, fishery, forestry, and food retail/ catering.

General Information

The Forecast takes into account the goals and priorities of Russia's social and economic development outlined by President Medvedev in his 2010 state-of-the-nation address as well as the Concept of the Long-Term Socioeconomic Development of the Russian Federation through 2020, also known as Russia's Strategy-2020. The Forecast is based on the statistics of Russia's social and economic development through January-July 2011 and development forecasts of Russia's federal and local government bodies and the Central Bank of Russia. The document outlines two "basic" development scenarios (moderately optimistic and conservative) and two "additional" scenarios (negative and optimistic) for Russia's economy as a whole. For more details on each of the scenarios please see section *Four Economic Development Scenarios* and Table 14 attached. The Forecast recommends that the moderately optimistic scenario be used for drafting Russia's Federal Budget for 2011-2014.

The forecast for the agricultural sector presented in the document and reported on below is based on the moderately optimistic scenario, which projects that the share of agriculture (including hunting and forestry) in GDP should stabilize at the level of 3.3-3.2% in 2011-2014 (see Table 15 attached).

Overall, according to MED, the Russian economy remains heavily dependent on the processes occurring in the global economy, with commodity prices, especially oil prices, being the most important factor, which largely determines stability of Russia's federal budget and the balance of payments.

The Forecast does not make it clear if the impact of Russia's accession to the World Trade Organization (WTO) was taken into account in the MED calculations of the outlook for 2012-2014. At the same time, the prospect of Russia's WTO accession is mentioned in chapters covering Customs and Tariff Policy, Machine-Building Industry, Forestry and Foreign Trade and the mention in the Forestry section is made in the context of the conservative scenario, thus indicating indirectly that it is the conservative scenario that possibly takes into account the impact of the WTO accession.

Table 1. Key Indicators of Russia's Economic Development in 2010-2014

(% to the respective period of the previous year)

Indicators	2010	2011	Forecast (moderately optimistic scenario)
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	actual	estimate	2012	2013	2014
Average Price of Urals Oil, \$ per barrel	78.2	108	100	97	101
Consumer Price Index	8.8	6.5-7.0	5.0-6.0	4.5-5.5	4-5
GDP	4.0	4.1	3.7	4.0	4.6
Industrial Production	8.2	4.8	3.4	3.9	4.2
Agricultural Production	-11.9	13.7	1.4	2.2	2.4
Fixed Capital Investment	6.0	6.0	7.8	7.1	7.2
Real Disposable Monetary Income	4.2	1.5	5.0	4.8	5.3
Real Wage	5.2	3.6	5.1	5.8	6.3
Retail Trade Turnover	6.3	5.3	5.5	5.3	5.5
Exports of Goods, \$ billion	400.4	527.5	533.1	535.9	565.3
Imports of Goods, \$ billion	248.7	340.0	397.4	444.6	486.1

Underpinning MED's forecast for the Russian economy are assumptions of global economy growth rates (see Table 16 attached), as well as separate forecasts for major economies such as the United States, Japan, China, and the Eurozone, as well as Russia's neighbors – the Commonwealth of Independent states (CIS) – Ukraine, Kazakhstan and Belarus (see Table 17 attached). Additionally, estimates of 2011-2014 production, supply and demand as well as prices for key commodities for Russia, namely oil, gas, steel, aluminum, copper, nickel, and wheat (see Table 2 below) are presented in the Forecast.

Table 2. Balance of Global Production and Consumption of Wheat

	2009	2010	2011	2012	2013	2014
Production, million metric tons (MMT)	683	653	677	685	694	706
Consumption, MMT	660	669	679	687	692	702
Carryover stocks, MMT	208	193	192	189	192	196
Exports, MMT	128	123	125	127	127	132
Sown area, mln ha	227	217	224	223	224	225
Structure of use, %						
Production of feed	19.2	18.9	19.5	19.5	19.3	19.5
Food	69.0	68.6	68.2	68.2	68.3	68.0
Biofuel	0.9	0.9	1.1	1.1	1.3	1.5
Other	11.2	11.6	11.2	11.2	11.1	10.9
Price, \$ per metric ton	193	237	295	250-270	250-280	260-300
Consumption per capita, kg	67	66	66	66	66	66

Source: FAO-OECD, USDA, forecast of the Ministry of Economic Development of the Russian Federation

Russia's Socioeconomic Development Priorities for 2012-2014

According to the Forecast, socioeconomic policies of the government of the Russian Federation in the medium term (2012-2014) are characterized as transitional in connection with completion of the post-crisis recovery and further increased focus on strategic measures set forth in Strategy-2020. In the coming years, along with its work towards fiscal consolidation, Russia will need to lay the groundwork for furthering its longer term interests, such as establishing a modern and innovation-based economy, integrated into the global economy.

The forecast spells out the following priorities of Russia's economic policy in the period:

- social development and investment in human capital;
- modernization of the defense industry and the armed forces;
- innovative development and support of high-tech sectors;
- economic diversification, infrastructure development (including modernization of agriculture and fishing industry (food industry), development of timber industry);
- balanced regional development;
- improved investment climate, development of competition and reduction of administrative burden on business;
- increased stability of the national financial system, reduction of the budget deficit and lower inflation;
- formation of the customs union and adjustment of the national economy to the WTO requirements.

Key Policy Measures Affecting Agriculture

Key measures of tax, customs, tariff and budget policy, planned for 2012-2014, are outlined in chapter 2.3 *Terms of Economic Development*.

Tax Policy

According to the Forecast, the government will continue raising excise tax rates on certain goods, in particular, on alcoholic, alcohol-containing and tobacco products, and alcoholic products stronger than 9% of ethyl alcohol by volume will be subject to faster excise tax increases compared to those containing less than 9% of ethyl alcohol by volume, as well as with beer and natural wines. As for tobacco products, given Russia's official goal of reducing tobacco consumption stated in the Concept of state policy on combating tobacco consumption for 2010-2015, excise taxes on such products are set to triple from 2011 to 2014 through gradual annual increases to reach the average level of taxation of tobacco products among countries in the European Region of the World Health Organization (in terms of purchasing power of the population).

Customs and Tariff Policy

Since the launch of the Customs Union between Russia, Belarus and Kazakhstan in 2010, Russia's customs and tariff policy has been subject to supranational decision-making procedures, under which the power to change the rates of import customs tariff and implement other customs and tariff measures was

handed over to the Customs Union Commission. Thus, Russia's customs and tariff policy will be determined by further development of the CU and the Common Economic Space (the next stage of the CU economic integration, facilitating the free movement of goods, services, capital and workforce, to be launched as of January 1, 2012), as well as Russia's potential accession to the WTO.

In the short term, MED foresees rapid import growth and a consistent reduction in the trade balance. Based on the estimated dynamics and structure of imports to Russia and its CU partners, Russia's average weighted rate of import tariff, taking into account concessions and preferences, is expected to decrease gradually from 9.64% in 2011, to 9.5% in 2012, 9.33% in 2013 and 9.15% in 2014. MED also expects that in case of WTO accession, Russia's average weighted import tariff will decrease an additional 0.8 percentage points from the first of year of the new tariff's implementation.

In the medium-term, Russia customs and tariff policy will be driven by the needs of economic modernization, including by means of customs and tariff mechanisms that could stimulate the growth of competitiveness of the national producers in the domestic and foreign markets. Hence, the following measures are planned in this area:

- Customs tariff escalation, improvement of its structure and other quality parameters;
- Introduction of new subheadings in the foreign trade commodity nomenclature for the purpose of differentiating the rates of import tariff on import sensitive goods
- Rapid response with customs and tariff policy measures to the opening or protection of markets for certain goods in case of economic feasibility;
- Complementary application of customs and tariff policy instruments and special safeguard measures for domestic market protection given the transfer to the supranational level of authority to conduct investigations and implement of anti-dumping, safeguard and countervailing duties;
- Improvement of the CU system of tariff preferences;
- Development of a unified procedure for the application of exemptions from the customs tariff for certain categories of goods imported to the CU;
- Improvement of the rules of origin of goods in the CIS;
- Complimentary application of state policy measures in the field of agriculture and the use on the agricultural market of the customs and tariff regulation instruments that have proven effective both in Russian and international practice.

Implementation of the stated priority customs and tariff policy measures in their entirety will be subject to stabilization on the domestic and world markets. MED notes that in case of an increasing risk of a new global financial crisis, the use of protectionist measures may be required.

According to MED, accession to the WTO will not change the main priorities of Russia's customs and tariff policy. However, WTO membership will establish strict limits for the tariff policy:

- All tariffs will be bound;
- Since Russia's tariff in force in 2002-2006 was used to establish Russia's ceiling rates, many import tariff rates will go back to their pre-crisis level;
- There will be a gradual liberalization of tariffs on most industrial goods, as well as a number of agricultural and food products.

In these circumstances, regulation of foreign economic activities should focus more on non-tariff measures, including safeguard and anti-dumping duties. Further improvement of customs administration, as well as employment by the customs authorities of the new forms of work, compliant with the standards and rules of the international trade system will also be needed.

As for export tariffs, in the medium term it will continue to perform its narrow regulatory functions, including removal of the rental component of the resource revenues to the budget. At the same time, the government will develop proposals to increase the fiscal component of the export duties on the globally traded commodities (other than oil and oil products) that are subject to significant price fluctuations.

Budget Policy

Measures of state support outlined in the State Program for Development of Agriculture in 2008-2012 play a key role in creating a value-added agricultural sector. The goals of the Program include creation of conditions for the introduction of modern technologies, improvement of agronomic culture and infrastructure.

Table 3. Agricultural Development Indicators

Indicator	2008		2009		2010		2011		2012	
	target	actual	target	actual	target	actual	target	estimate	target	forecast
Agricultural production index, % y-o-y	103.8	110.8	103.9	101.4	104.1	88.1	104.1	113.7	104.1	101.4
Production of livestock and poultry (live weight), MMT	9.0	9.3	9.5	10.0	10.1	10.6	10.8	11.0	11.4	11.5
Share of Russian meat and meat products production in the total supply, %	61.1	61.2	63.5	64.2	65.7	67.5	68.1	71.4	69.6	74.4
Production of milk, MMT	33.0	32.4	34.0	32.6	35.0	31.8	36.0	31.2	37.0	31.1
Share of Russian milk in the total supply, %	78.3	77.8	79.2	78.2	79.9	76.3	80.4	74.9	81.1	74.3
Purchase of tractors, thousands	23.0	23.9	29.0	18.8	35.0	16.4	41.0	15.2	48.0	16.6

As a consequence of the financial and economic crisis, the drought, and intense competition from imported products there is a noticeable gap between the main parameters of the State Program for Development of Agriculture in 2008-2012 and the actual indicators of the agricultural sector development (see Table 3 above). As a result, agricultural production will grow an estimated 14% in 2012 over 2008, below 21.7% that was targeted for the period by the State Program. Production of milk is significantly behind the State Program target, while the share of Russian meat and meat products production in the total supply in 2012 may exceed the target by 5.2 percentage points.

A significant factor in shaping the environment and targets of agricultural development should be the launch in 2013 of a new state program for development of agriculture until 2020. In addition to the traditional instruments of state support, a number of new measures will be added, including development of small businesses, support for development of agricultural processing industries, development of infrastructure and logistics for the agri-food market, development of land reclamation and others. The new state program envisions a new approach to the state support with an emphasis on comprehensive sub-programs for individual sectors, covering all stages of the technological process from production to sales and focusing on the final demand for finished products.

Federal funding of agricultural development is estimated to total at least 125 billion rubles (about \$4.2 billion) in 2011, at least 130 billion rubles (\$4.3 billion) in 2012, and 118 billion rubles (\$3.9 billion) a year at a minimum in 2013-2014. These numbers are 20-30% below the needed level due to budget constraints, hence the share of state support for agricultural organizations and private farms in relation to the volume of their production tends to decrease (8.6% in 2010 versus 5.8% in 2014).

Government support will continue to focus on the interest-rate buy-downs for agricultural producers. However, in the medium term, the scale of subsidies will slowly decrease as new support mechanisms will be employed to target the increase of marketability of production (e.g. subsidizing production of 1 liter of marketable milk with the relevant quality characteristics) and increased access to capital for farmers (mortgage operations).

Agriculture

According to MED, growth of Russian agricultural production in 2011 is expected to surpass the level reached in 2009, thus compensating for the losses caused by the 2010 drought. Agricultural production in 2014 should increase by 15-21% over 2010, given the low base effect.

MED believes that stable growth in real incomes, external demand, and realization of export potential (the use of competitive advantages) create a favorable environment for sustainable growth of the agricultural sector, improvements in its efficiency, and import substitution.

Table 4. Production of Main Agricultural Products, %

Name	2010 actual	2011 estimate	forecast			2014 over 2010, %
			2012	2013	2014	
Agricultural production index	88.1	113.7	101.4	102.2	102.4	120.7
Grain (clean weight)	62.8	150.9	101.6	101.6	105.3	164.0
Sugar beet	89.4	166.7	87.8	107.0	101.5	159.0
Sunflower seeds	82.8	145.5	96.1	102.0	101.3	144.3
Potato	67.9	132.4	100.7	100.4	100.4	134.3
Vegetable	90.5	108.0	100.8	100.8	101.1	110.9
Livestock and poultry (slaughter weight)	105.8	104.4	104.4	104.0	103.9	117.8
Milk	97.8	98.0	99.5	100.5	101.0	99.0
Eggs	103.0	101	100.5	100.5	100.5	102.5
Index of production of food products, including drinks and tobacco	105.4	103.7	102.2	103.0	103.1	112.5
Sugar	93.6	141.4	80.7	104.6	101.1	120.7
Unrefined vegetable oils	95.8	104.9	109.5	103.6	102.5	122.1
Meat and sub-products – total	115.0	108.0	106.9	105.4	105.2	128.0
Cheese and cheese products	101.2	99.0	101.0	101.0	101.5	102.5

MED identifies the following key factors determining the projected dynamics of the agricultural sector in 2012-2014:

- increased demand due to growth in real disposable incomes;
- implementation starting in 2013 of a new State Program for Development of Agriculture and Regulation of Commodities Markets, including measures to support key sectors of the food industry and develop land reclamation, infrastructure and logistics for the agri-food market;
- development of the agricultural sector of the economy with the help of considerable state support;
- application of innovative technologies and modernization of the processing industry;
- rapid response by the government to changes in the agri-food market;

- realization of the export potential of the food industry;
- development of relations within the Common Economic Space.

Measures of innovative development of agriculture will be reflected in the strategy for innovative development of agriculture and a program for development of biotechnology in the Russian Federation until 2020 (BIO 2020), which will create the preconditions for high-quality technological change in agriculture. Technological change and the new state support measures will have a stabilizing effect on the domestic market and will be a factor for attracting investment in agriculture.

In addition, MED says that according to FAO estimates, the continued trend of high-level prices for agricultural products on the global markets will create incentives for investments in production. The global price trends will affect the price situation in the Russian agricultural sector, which is integrated into the architecture of the global market. Besides, domestic prices for agricultural products will remain high in connection with the planned increase in prices of “natural monopolies”. Prices of producers of agricultural products could rise by 20-30%.

At the same time, according to MED’s Forecast, investment in agriculture will fail to reach the pre-crisis levels, totaling only 85.1% of the 2007 level in 2014, due to continuing influence of the factors that inhibit investment growth, such as the effects of the financial crisis, financial losses due to the drought, and a lack of available markets.

In the crop sub-sector, dependence on climatic conditions results in the permanently high level of volatility of its growth rates. The drought in 2010 forced the government to reconsider the priorities of the state support and allocate federal funds to restore the land reclamation system of the country starting in 2013. MED believes that in the future, the land reclamation activities should help partially neutralize the effect of climatic risk in agriculture.

Grain

Following the drought in 2010 that severely affected the grain harvest and prompted a ban on grain exports, which lasted until the new marketing year (July 1, 2011), Russia’s grain exports in the 2010/2011 marketing year totaled 3.9 MMT, according to MED.

MED notes that the growth of domestic prices for grain in the second half of 2011 was constrained by Russia’s high carry-over stocks of grain, as well as reduced prices on the global market in anticipation of exports of the Black Sea and Kazakh grain. According to the Ministry, the expected grain harvest of 92 MMT should also have a stabilizing effect on the domestic grain market, and it has already led to a significant drop in prices and a widened gap with global prices. Taking into account the potential effect of purchasing interventions and export support, the domestic price for wheat (EXW, elevator) at the end of 2011 is expected to reach 5.3 thousand rubles (about \$180) per metric ton (although it can be significantly lower in some regions of Siberia and the Urals).

In the medium term, MED expects Russian grain exporters to regain their positions in global trade, which were lost during the export ban. According to MED, Russia’s grain production could increase 1.6 times (up to 100 MMT) in 2014 over 2010 and export volumes should stabilize at the level of 20-25 MMT. In the case of unfavorable external economic conditions, natural anomalies, and high production

costs, MED forecasts that Russia's grain harvests in the medium term will not exceed 90 MMT on the average.

Production of flour and cereals is expected to grow moderately in the forecast period, increasing in 2014 over 2010 by 4.6% and 4.7%, respectively. Development of the market is driven by demand from the bakery and confectionery business, as well as catering and retail sectors. Exports of flour are expected to increase substantially, as its export potential exceeds the current level several times.

Sugar

MED notes that in 2011 the sugar beet industry saw an unprecedented expansion of sown area, triggered by the high prices of the previous period and the restoration of productivity to long-term averages. These were the main factors behind the expected record-high harvest of sugar beets (about 37 MMT) in 20 years. According to MED, expectations of a large harvest form the downward price trend for sugar and sugar beets. Prices for sugar beets may drop by an estimated 15-20% compared to the previous season, which will have a negative impact on the ability to maintain the acreage in 2012 at the 2011 level.

The record-high harvest of sugar beets in the current season has led to a new record for production of beet sugar - 4.4 MMT, or 65.7% of the total sugar production. Given the growth in imports of raw sugar as a result of early introduction of a lowered rate of import tariff on raw sugar of \$50/MT, which also caused an increase in the raw sugar production, MED expects Russia's total sugar production to rise by 41.4% in 2011. As a result, according to MED's Forecast, sugar stocks will be high, pushing wholesale prices down, and a large supply of the product on the market could lead to a reduction in the sugar production in 2012.

Table 5. Sugar Supply, MMT

Name	2010 actual	2011 estimate	2012	2013	2014	2014 over 2010, %
			forecast			
Sugar Supply, total	7.6	8.9	8.7	8.7	8.6	112.7
Production	4.7	6.7	5.4	5.7	5.7	120.7
Imports	0.3	0.3	0.3	0.3	0.3	87.6
Use	5.7	5.9	5.9	6.0	6.1	107.0
Domestic consumption	5.4	5.5	5.6	5.7	5.7	105.2

MED lists the following fundamental factors of investment attractiveness of the beet sugar production:

- the program for development of the beet sugar complex (including interest rate subsidies for the construction and modernization of sugar refineries and the construction of the seed processing facilities, partial compensation for the costs of mineral fertilizers and crop protection chemicals),
- the budget support measures,
- the current raw sugar import regime,
- the producers' interests in obtaining optimal profitability associated with the marketing of beet sugar.

In the medium term, MED expects that the trend towards redistribution of production in favor of beet sugar production will strengthen. Further plans to increase sugar production will be interlinked with the

expansion of exports to the CIS countries and Central Asia.

Oilseeds

MED believes that high margins on oilseeds continue motivating agricultural producers to cultivate them. According to MED's Forecast, a bumper crop of around 8 MMT of sunflower seeds was expected in 2011 due to a substantial expansion of cultivated areas. The expectation of a large harvest of oilseeds in 2011 coupled with the commissioning of new refining capacity should support the production of vegetable oils at a high level, which will help increase exports of finished products.

The demand for rapeseed and soybeans from the global market and the livestock industry, together with the favorable pricing prospects, signal the need to increase production of these agricultural products.

In the medium term, underutilized production capacity and the desire of industrial enterprises to increase their global market share of sunflower oil will keep up their interest in cultivating sunflower seeds. As a result, under favorable conditions, Russia's production of sunflower seeds will probably not fall below 7 MMT a year.

Production of oils from seeds will increase by 13-22% in 2014 over 2010, depending on the projected harvest of oilseeds, while exports are expected to increase by a factor of 1.7 in 2014 over 2010. Sunflower oil imports are constrained by the availability of domestic supply, which almost completely satisfy the needs of domestic consumers.

Animal Products

In the medium term, MED expects animal products to have slight majority in the structure of Russia's agricultural production with a share of 52%. Production of animal products is projected to grow by 10% in 2014 over 2010. Conservative scenario developments in the sub-sector are possible in the cases of unfavorable external market conditions and existence of epizootic risk. The risk of African swine fever continuing to spread in the future means loss of livestock, quarantine of territories, and disruption of trade.

MED believes that a significant price increase is unlikely given "some global overproduction" of certain animal products (poultry, milk) in 2012. The Ministry forecasts that in 2013-2014 prices for animal products may start outpacing inflation rates due to an increase in demand (for red meat and high quality dairy products), and also because of the rise in price of feed, should grain prices rise. Besides, according to MED, the upward trend in the global prices for animal products may increase, particularly in case of continued growth of energy prices.

Meat and Poultry

MED estimates that production of livestock and poultry for slaughter (in slaughter weight) should grow by 4.9% y-o-y in 2011, mainly due to production of poultry and pork benefiting from an expected decline in imports and consumption growth.

Table 6. Meat and Meat Products Supply and Distribution, MMT

Name	2010 actual	2011 estimate	2012	2013	2014	2014 over 2010, %
			forecast			
Meat supply, total	10.6	10.5	10.6	10.8	11.0	103.8
Production	7.2	7.5	7.9	8.2	8.6	119.5
Imports	2.6	2.3	2.1	1.9	1.9	70.4
Use	9.9	9.9	10.0	10.2	10.4	105.6
Domestic consumption	9.8	9.8	9.8	10.0	10.2	104.7

The Ministry states that in the future, given the “saturation” of Russia’s meat market, insufficient infrastructure and existing problems with sales, production growth in key sub-sectors of livestock production will slow down. In particular, production of poultry and pork in 2014 over 2010 should grow by 33% and 21%, respectively (for comparison, poultry production increased 1.8 times in 2010 over 2006, and pork - 1.4 times).

MED hopes that extensive production growth should give way to its intensification, aimed at meeting market demand, both in volume and in quality. According to MED, “saturation” of the market with pork and poultry products will signal producers to redirect investment flows into construction of infrastructure facilities, technology improvement, and market research.

MED’s Forecast stipulates that the rising cost of grain will affect poultry and pork production costs (in particular, at technologically-weak companies and private farms), while prices on these products will be constrained by consumer demand and supply of imported products. As for a government policy measure, over the medium term, the mechanism of meat quotas will remain in place, narrowing the market for imported products. MED expects that the share of pork imports in its supply in 2014 will account for 17.3% versus 25% in 2010, for poultry - 8.3% versus 18.2%.

Despite the recovery of consumer demand and significant government support, production of cattle is estimated to decrease by 2.3% in 2014 over 2010. Thus, the share of cattle in the structure of livestock and poultry production should be redistributed in favor of pork and poultry.

Dairy

According to MED, in recent years, Russia’s dairy sector was subject to a number of negative factors that affected its development, in particular, increased competition from imported dairy products. MED notes that decline in consumer demand due to the crisis, growth of production costs, significant seasonal fluctuations in prices of milk, and a drought, which has reduced the number of cows due to increased feed costs affected milk production in 2011 and will continue to affect it in the medium term. Milk production is expected to decrease by an estimated 1% in 2014 over 2010.

As a result of increased cattle costs, MED expects that the tendency to reduce the number of cows will persist, especially in households, which account for a significant share of milk production among all types of entities (45-48%). In recent years, there has been a significant increase in milk yields as part of production intensification. However, growth in milk yields per cow does not compensate for the decline in milk production, which occurs due to reduced cow numbers.

The decline in milk production and increased production costs have led to a higher production cost per liter of milk, which affects the entire food production chain. One of the tools for maintaining price

stability in the dairy market is an agreement among producers and processors that agreed mutually acceptable minimum and maximum price levels for raw milk, which should help smooth out seasonal price fluctuations in the future.

Renewed growth in consumption of dairy products after the crisis coupled with a deficit of domestic production of raw materials in the medium term will determine the growth of imports, mainly from the CIS countries, which enjoy a free trade regime. The share of domestic dairy products in total supply will go down from 76% in 2010 to 74% in 2014. Per capita consumption will increase from 245kg in 2010 to 249-250kg in 2014.

Table 7. Milk and Dairy Products Supply and Distribution, MMT

Name	2010 actual	2011 estimate	2012	2013	2014	2014 over 2010, %
			forecast			
Milk supply, total	41.7	41.7	41.8	42.1	42.7	102.3
Production	31.8	31.2	31.1	31.2	31.5	99.0
Imports	8.0	8.7	9.1	9.3	9.4	117.6
Use	39.9	40.0	40.2	40.4	40.7	102.0
Domestic consumption	35.1	35.2	35.4	35.5	35.7	101.8

The situation on the world dairy market indicates that prices are not expected to decrease. However, despite the expected increase in prices on the global dairy market, imported goods will be cheaper than domestic product, and there will still be a gap between domestic prices and import prices of dairy products, which affects Russia's production of dairy products.

Fishery Sector

Russia's fishing industry continued to operate in the new environment that was formed in 2008-2009 when a number of legislative acts determining the industry's development in the mid- and long-term were adopted. The government policy has not only allowed the stabilization in the industry but also created conditions for increasing the domestic production of fish products.

In 2011, Russia's catch (harvest) of aquatic biological resources is expected to grow 1.8% y-o-y, to 4,100 metric tons (MT), while production of processed and canned fish and fish products should increase by 5% y-o-y, to 3,570 MT. According to preliminary estimates, average per capita consumption of fishery products will rise to 17.3 kg in 2011, up 4% y-o-y.

Development of the fishing industry in the forecast period will be supported by implementation of the federal target program "Improving the efficiency and development of the resource potential of the fishery complex in 2009-2014," and from 2013 – by the "State program for development of the fishing industry until 2020".

The main directions of economic policy in the industry are:

- rational use of available production capacity;
- financial turnaround of enterprises of all types of ownership, revitalization of the domestic commercial shipbuilding industry;
- development of far-off fishing, including beyond the exclusive economic zone of the Russian Federation;

- development of aquaculture.

Development of the fishing industry in the medium term will be achieved through a series of measures designed to:

- further improve the mechanisms of sustainable and long-term management of aquatic bio-resources,
- ensure the necessary state support in the area of reproduction and protection of aquatic bio-resources, safety of navigation, research, comprehensive measures for development of artificial reproduction of aquatic bio-resources and aquaculture;
- support enterprises through interest-rate buy-down loans for construction, acquisition, and modernization of fishing vessels;
- maximize the use of leasing for fishing fleet renewal;
- develop instruments of customs tariff regulation for imports of marine equipment, processing equipment, fishing equipment, and equipment for aquaculture;
- expand international cooperation on fishery and create conditions for development of the domestic market of fishery products.

Under the forecast, Russia's fish catch should grow to 4,860 MT in 2014, up 20.7% over 2010. Production of processed and canned fish and fish products is estimated to reach 4,164 thousand MT in 2014, up 22.5% over 2010.

Table 8. Production of Major Products Fishing Industry, %

Name	2010 actual	2011 estimate	forecast			2014 over 2010, %
			2012	2013	2014	
Catch (harvest)	108.3	101.8	104.9	105.8	106.8	120.7
Fish and fish products processed and canned	102.7	105.0	105.8	105.0	105.0	122.5

Exports of fishery products have been growing at a moderate pace so far this year and are expected to hit 1.7 MMT in 2011, up 5.5% y-o-y, reaching 2.0 MMT in 2014, up 23.2% over 2010. Simultaneously, imports of fishery products are declining and are estimated to fall to 980.2 thousand MT in 2011, down 1.4% y-o-y, and to 937.7 thousand MT in 2014, down 5.7% over 2010. The physical volume of fish imports has been reducing due to a decrease in imports of frozen herring and mackerel. At the same time, the share of imports that are in fact re-exports will remain stable due to long-term contracts between domestic fishing companies and foreign investors, as well as different levels of labor costs.

Current economic policy and implementation the federal target program as well as the drafted state program for the sector until 2020 will contribute to achieving the following indicators:

Table 9. Key Indicators of Fishing Industry Development

Indicator	2010	2011	2012	2013	2014
Release of aquatic bio-resources into the wild and reservoirs, mln. number	9,000	9,045	9,090	9,135	9,180
Aquaculture production, thousand MT	140	140	170	200	230
Average per capita consumption of fish products in the Russian Federation, kg	14	14.6	15.3	16.0	18.0
Availability of coastline control in order to stop violations of aquatic bio-resources harvesting, %	70.0	78.0	87.0	99.0	99.0
Replacement rate of industry's fixed assets, %	7.7	7.9	8.0	9.0	9.1
Share of domestic fish products on domestic consumer market, %	71.4	73.1	75.8	80.1	80.5

Fishing industry development should focus on such priorities as catch of aquatic bio-resources in the open part of the oceans and inland waters as well as commercial cultivation.

At the same time, as MED notes, given that the industry's production depends on natural resources (aquatic resources) that are heavily influenced by the natural environment as a whole and have cyclical growth of population that cannot always be accurately projected, a reduction in the number of key commercial species of aquatic bio-resources is likely. This can affect both the catch and production of fish products. Similarly, in case of insufficient state support for the industry, the rundown state of fixed assets, particularly in the fishing fleet, and a lack of investment resources in the majority of companies, will not allow the industry to achieve the planned growth in the coming years. Under this scenario, fish catch would not exceed 4.3 MMT in 2014, up 6.0% over 2010, while production of processed and canned fish and fish products would total 3.7 MMT in 2014, up 9.0% over 2010.

Forestry

According to MED's Forecast, the main risks for Russia's forestry industry in the medium and long term include: (1) a possible lack of capacity for deep processing of wood, (2) a low level of innovation activity and investment attractiveness, and (3) the quality and competitiveness of Russian products, including on international markets.

MED notes that Russian products are inferior to foreign analogues because of the outdated technologies that are unsafe for the environment and more resource-intensive. There is a lack of facilities for deep processing in the industry, while existing facilities operate almost at full capacity (capacity utilization reached 82.4% in the pulp and paper industry in 2010, and 95.5% in cardboard production). At the same time, Russia's pulp and paper industry has a considerable potential, as, according to MED, Russia consumes about 50 kg of paper and cardboard per capita, compared to 300 kg in the United States and more than 400 kg in Finland.

Table 10. Production of Major Forestry Products, %

Product	2010 actual	2011 estimate	Forecast			2014 over 2010, %
			2012	2013	2014	
Wood processing and production of wood products, %	111.4	106.5	104.7	105.5	106.1	124.8
Sawn timber and lumber, %	105.1	106.6	105.8	106.2	106.7	127.8
Fiberboard, %	106.0	106.1	105.4	106.3	107.3	127.5
Particle board, %	119.3	109.0	105.1	106.4	107.0	130.4
Plywood, %	125.9	108.3	104.5	105.6	106.0	126.7
Industrial Wood, %	109.8	107.5	103.9	104.0	105.4	122.4
Pulp and paper production; publishing and printing activities, %	105.9	101.3	102.7	103.3	103.8	111.6
Commercial cellulose, %	103.4	105.5	103.3	104.0	104.6	118.7

Development of Russia's forestry industry is currently determined by dynamics of the external environment with China and the European Union (mainly Finland) being the major importers of Russian unprocessed wood.

In the medium term, growth in exports of unprocessed wood is expected to be low (less than 3%), and by 2014 its share in total exports of wood and wood products should go down to 12%, representing an 8% decrease compared to 2010. At the same time, exports of forestry products with a higher degree of processing are expected to continue to grow fast: exports of particle board should increase by 7% y-o-y in 2011 (to reach 135% in 2014 over 2010), exports of sawn timber and lumber - about 7% (129%), and exports of cellulose - 4% (120%).

Imports of the following forestry products, that are not produced in Russia, are expected to growth at faster rates: high-tech wood-based panels (imports of particle board should increase by 9% y-o-y in 2011 and by 52% in 2014 over 2010; imports of fiberboard should grow by 6% and 29%, respectively), high-tech kinds of paper and paperboard (imports should grow by 5% y-o-y in 2011 and by 14% in 2014 over 2010), including coated paper and paperboard, tissue-based hygiene products, various types of paper and board packaging with multicolor print, film, and water-repellent coatings.

Table 11. Growth of Physical Volume of Exports and Imports of Forestry Products, %

Name	2010 actual	2011 estimate	Forecast			2014 over 2010, %
			2012	2013	2014	
Exports						
Unprocessed wood, %	98.2	100.8	101.9	103.9	104.9	111.9
Processed wood and wood products, %	108.2	106.8	104.1	104.6	105.2	122.4
Pulp and paper production; publishing and printing activities, %	105.2	102.3	103.2	103.9	104.2	114.2
Imports						
Processed wood and wood products, %	119.3	104.0	105.3	105.9	105.4	122.3
Pulp and paper production; publishing and printing activities, %	108.3	104.7	104.8	105.4	106.1	122.8

The Russian forestry industry is entitled to the following subsidies from the federal budget:

- interest-rate buy-downs on loans received by the forestry industry in the Russian credit institutions in 2008-2009 for off-season reserves of timber, raw materials and fuel. In 2011-2013 it is planned to allocate 650 million rubles (about \$21.7 million) of the federal budget funding annually for this purpose (176 million rubles (\$5.9 million) were claimed by the industry in the 1st half of 2011);
- interest-rate buy-downs on loans of up to 5 years received by Russian companies from certain industries (the agricultural and tractor machine-building, forestry industry, engineering for oil and gas industry and machine-tool industry) from the Russian credit institutions in 2008-2011 for technical upgrade. In 2011-2013 it is planned to allocate 1 billion rubles (\$33.3 million) annually for this purpose (forestry industry claimed 75 million rubles (\$2.5 million) from the established limit in the 1st half of 2011);
- interest-rate buy-downs on loans received by Russian exporters of high-tech industrial products from the Russian credit institutions, including exporters of wood and paper products.

Should the current trends persist, the moderately-optimistic scenario foresees moderate growth of production in the industry in the medium term starting from 2011, due mainly to the following factors determining the forestry industry's development:

- additional increase in fixed investment;
- improvement of terms of credit and leasing for woodworking equipment;
- implementation of the promising investment projects for the technological modernization of the forestry industry;
- implementation of the state support measures in the forestry industry.

According to MED, 2011-2014 should see continued increase in domestic consumption of forestry products. At the same time, forestry production growth rates should increase due to launch of a number of new production facilities built as part of priority investment projects in the area of forest exploitation. The Ministry of Industry and Trade has so far approved 95 investment projects for an approximate 413 billion rubles (\$13.8 billion) with a projected processing capacity of about 73 million m³ per year. Seventeen of the priority investment projects with a total investment of 58.8 billion rubles (\$2.0 billion) and allowable cut of 7 million m³ have already been commissioned. Overall, some 12 priority investment projects are expected to be implemented each year. Additionally, a number of projects are currently implemented with the use of other types of state support, such as investments through the state-owned Vnesheconombank (a wood processing facility for production of particle board and sawn lumber in the Khabarovsk Territory; to be launched in 2011) and Investment Fund (upgrade of the wood-working facility in the Smolensk Region; to be launched in 2012).

Development and modernization in the pulp and paper industry is driven primarily by the implementation of a small number of projects for modernization of existing facilities undertaken by large owners. Such projects include the modernization of the Bratsk Pulp and Paper Mill with an estimated investment of about 20 billion rubles (\$670 million), to be commissioned in 2012; and an import-substitution project to organize production of light-weight coated paper on the Kama Pulp and Paper Mill, to be commissioned in 2011.

Investment in wood processing and manufacturing of wood products is expected to increase by more

than 80% in 2014 over 2010, while investment in the pulp and paper production and publishing and printing activities - by 55.5%.

Under MED's conservative scenario, the reduction of export duties on raw timber as part of Russia's accession to the WTO could serve as an incentive to increase the volume of logging. Thus, a significant reduction in the rates of export duties for timber may lead to lower investment in the forestry industry, stagnation in the processing segments of the industry (especially in the sawn lumber production), and a sharp increase in exports of unprocessed wood.

Food Retail and Catering

According to MED, despite the growth in Russia's per capita consumption of certain foods, such as meat and meat products, milk and dairy products, vegetable oils, vegetables, and fruits, Russia lags far behind developed countries in this indicator. For meat and meat products Russia's per capita consumption is more than 2 times less than in the United States, 1.5 times less than in France and Austria; for fruits - more than 2 times less than in the United States, the Netherlands, and Germany.

Table 12. Turnover of Retail Trade and Catering (y-o-y, %)

	2009	2010	2011 estimate	forecast			2014 over 2010, %
				2012	2013	2014	
Retail trade turnover	-5.1	6.3	5.3	5.5	5.3	5.5	23.2
Food	-1.8	5.1	1.2	2.2	2.5	2.3	8.4
Non-food	-8.2	7.6	9.1	8.3	7.9	8.4	38.2
Catering turnover	-12.7	2.8	5.2	5.7	5.4	5.6	23.8

The structure of sales of food products in 2012-2014 will be changing in favor of more expensive products. Thus, the share of meat and poultry, fish products, cheese, vegetables, fruits, and berries will increase at the expense of bread and bakery products, alcoholic beverages, and sugar.

Table 13. Sales of Certain Food Products (y-o-y, %)

	2009	2010	2011 estimate	forecast			2014 over 2010, %
				2012	2013	2014	
Food	-1.8	5.1	1.2	2.2	2.5	2.3	8.4
including:							
Meat (including poultry)	-5.0	5.3	3.1	3.2	3.3	3.2	13.3
Fish and seafood	-4.1	7.4	4.2	4.3	4.4	4.2	18.3
Dairy products	1.5	4.9	1.7	2.3	2.4	2.3	9.0
Fresh vegetables	4.3	6.0	-2.6	1.8	2.0	2.0	3.1
Alcohol drinks and beer	-3.0	-3.6	2.9	2.2	2.1	1.8	9.3

Despite the downward trend, the share of sales through retail and open-air markets in the structure of retail trade turnover will remain quite high in the forecast period, totaling about 10% of the turnover of food products. Some Russian regions plan to build new agricultural markets, which should help increase sales of domestic agricultural producers.

Attachments

Four Economic Development Scenarios

The moderately optimistic scenario reflects a relative increase in competitiveness of the Russian economy (demonstrated by a stronger trend towards import-substitution) and improved investment climate with a moderate increase in government spending on infrastructure and human capital in 2013-2014. The scenario is based on relatively favorable assessments of external conditions: the global growth recovery rate of 3.7 - 4.0% per year and the stabilization of prices for Urals crude in the range of \$97-101 per barrel. Russia's GDP growth in 2012-2014 is expected at 3.7% - 4.6%.

The conservative scenario implies the preservation of low competitiveness in relation to imports and lack of capital inflows amid slow recovery of investment activity and a reduction of real government spending on development. Under the conservative scenario annual growth rates of the Russian economy in 2012-2014 are estimated at 2.8% - 3.8%, which is below an expected rate of growth of the world economy. Further versions of the scenario with different dynamics of oil prices and global growth have been developed but they are not presented in the Forecast.

The negative scenario is characterized by deterioration of the dynamics of the global economy (on the verge of stagnation in developed countries), although it does not involve the resumption of the recession. Under these circumstances, the price of oil is expected to decrease to \$ 80 per barrel in 2013. Given the high dependence of the Russian economy on external economic conditions, this scenario exacerbates the risks of stability of the banking system, the balance of payments and the overall level of confidence of economic agents. Russia's economic growth is expected to slow to 1.5-2.5% in 2012-2013 and to 3.7% in 2014 - with a significant weakening of the ruble. An additional version of this scenario, implying the resumption of global recession and the fall of oil prices to \$60 per barrel in 2012 was considered. This additional scenario (which is not included in the Forecast) could see Russia's GDP contract by 0.5% - 1.4% with a significant devaluation.

The optimistic scenario reflects the continuation of relatively high rates of the global economic growth and oil prices in 2012-2013 at \$105-109 per barrel with an acceleration of growth to \$113 per barrel in 2014. Under the scenario, Russia's GDP in 2012-2014 may grow up to 0.2 percentage points faster than the baseline moderately optimistic scenario and range between 3.9% and 4.6% per year.

Table 14. Key Indicators of Russia's Socioeconomic Development Forecast in 2010-2014

	2010	2011	2012	2013	2014
Price of Urals Oil (global), \$ per barrel					
optimistic	78.2	108	105	109	113
moderately optimistic		108	100	97	101
conservative		108	100	97	101
negative		108	96	80	80
GDP, growth rate in %					
optimistic	4.0	4.1	3.9	4.2	4.6
moderately optimistic		4.1	3.7	4.0	4.6
conservative		4.1	2.8	3.3	3.8
negative		4.1	2.5	1.5	3.7
Industrial Production, %					
optimistic	8.2	4.8	3.5	4.1	4.3
moderately optimistic		4.8	3.4	3.9	4.2
conservative		4.8	2.1	3.0	3.0
negative		4.8	2.3	3.7	3.8
Fixed Capital Investment, %					
optimistic	6.0	6.0	8.4	7.8	7.2
moderately optimistic		6.0	7.8	7.1	7.2
conservative		6.0	6.4	6.0	5.9
negative		6.0	6.0	1.5	3.7
Real Wage, %					
optimistic	5.2	3.6	5.2	6.2	6.3
moderately optimistic		3.6	5.1	5.8	6.3
conservative		3.6	4.0	3.9	4.0
negative		3.6	3.0	2.6	2.6
Retail Trade Turnover, %					
optimistic	6.3	5.3	5.8	5.9	5.6
moderately optimistic		5.3	5.5	5.3	5.5
conservative		5.3	4.9	4.8	4.8
negative		5.3	4.5	2.0	2.6
Exports of Goods, \$ billion					
optimistic	400.4	527	552	584	619
moderately optimistic		527	533	536	565
conservative		527	533	536	565
negative		527	492	443	441
Imports of Goods, \$ billion					
optimistic	248.7	340	401	458	512
moderately optimistic		340	397	445	486
conservative		340	392	435	475
negative		340	378	371	385

Table 15. Structure of Russia's GDP by types of Economic Activity, %

	2009	2010	2011	2012	2013	2014
				forecast		
GDP	100	100	100	100	100	100
Agriculture, hunting and forestry	3.9	3.3	3.3	3.3	3.2	3.2
Fishery and aquaculture	0.2	0.2	0.2	0.2	0.2	0.2
Extraction of natural resources	7.8	8.9	9.6	9.2	8.7	8.6
Processing industries	12.7	14.1	14.9	14.9	15.1	15.5
Production and distribution of power, gas and water	3.5	3.6	3.5	3.5	3.6	3.6
Construction	5.4	4.9	4.8	5.0	5.2	5.4
Wholesale and retail trade; repairs of vehicles, household and personal appliances	15.8	15.7	15.1	15.1	15.0	14.7
Hotels and restaurants	0.9	0.8	0.8	0.7	0.7	0.7
Transport and communications	8.4	8.4	8.0	8.1	8.2	8.2
Financial services	4.4	3.8	3.4	3.3	3.3	3.3
Real estate operations, rent and services	10.6	9.8	9.2	9.5	9.6	9.7
Government, military and social security	5.7	5.3	4.7	4.9	4.9	4.7
Education	2.9	2.6	2.4	2.4	2.3	2.2
Healthcare and social services	3.5	3.2	2.9	2.9	2.8	2.7

Table 16. Global Economy Growth Rates, %

	Scenario	2008	2009	2010	2011	2012	2013	2014
World	moderately optimistic/conservative	3.1	-0.6	5.0	3.8	3.7	3.5	4.0
	negative					3.4	2.9	3.5
	optimistic					4.5	4.2	4.7
	stagnation					2.4	1.8	2.8
USA	moderately optimistic/conservative	0	-2.6	2.8	1.6	2.0	1.6	2.8
	negative					1.5	0.8	1.7
	optimistic					2.5	2.5	3.0
	stagnation					0.5	0.0	1.0
Eurozone	moderately optimistic/conservative	0.9	-4.1	1.7	1.6	1.1	1.0	1.4
	negative					0.7	0.6	1.2
	optimistic					1.8	1.8	1.9
	stagnation					0.3	0.0	0.4
Japan	moderately optimistic/conservative	-1.2	-6.3	4.0	-0.5	2.6	1.6	1.7
	negative					2.0	0.7	1.0
	optimistic					3.3	2.2	2.2
	stagnation					1.8	0.5	1.2
China	moderately optimistic/conservative	9.2	8.7	10.3	9.0	8.0	7.8	7.8
	negative					7.5	7.3	7.2
	optimistic					8.5	8.2	8.3
	stagnation					6.0	5.0	6.5
CIS (ex Russia)	moderately optimistic/conservative	5.5	-6.6	4.6	5.0	3.4	5.0	4.6
	negative					2.3	1.6	1.9
	optimistic					6.0	3.5	5.7
	stagnation					1.0	0.5	0.8

Table 17. Economic Development Forecast for CIS Countries

In % to the previous period unless indicated otherwise	2009	2010	2011	2012	2013	2014
Ukraine						
Real GDP	- 15.1	4.2	4.8	4.7- 6.5*	4.8- 6.5*	5.0- 8.0*
Industrial production index	- 21.9	11.2	9.2	7.5	6.7	5.9
Fixed capital investment	- 50.5	4.9	8.8	10.3	6.1	5.4
Retail trade turnover	- 15.7	4.7	9.6	8.8	5.8	6.2
Consumer Price Index	15.9	9.4	10.7	9.7	7.7	7.0
Current account balance, % of GDP	-1.5	-2.1	-3.9	-4.4	-4	-4.3
<i>* official optimistic forecast</i>						
Kazakhstan						
Real GDP	1.2	7.0	5.0- 7.0*	4.8	4.7	4.8
Industrial production index	1.7	10.0	4.9	4.6	3.7	4.2
Fixed capital investment	2.1	3.0	9.2	3.6	2.7	3.2
Retail trade turnover	-2.0	9.3	6.6	4.8	4.4	4.9
Consumer Price Index	7.3	7.1	8.1	6.1	4.3	4.5
Current account balance, % of GDP	-3.8	2.9	1.4	-0.1	-0.2	-0.3
<i>* official forecast</i>						
Belarus						
Real GDP	0.2	7.6	1.4-5	-4 -1	-1-+2	2-4
Industrial production index	-2.8	11.3	3.1	2.0	4.0	5.0
Fixed capital investment	8.6	8.4	7.1	-8.5	1.0	3.7- 4.5
Retail trade turnover	- 12.0	10.3	5.3	-6.7	1.2	2.4- 3.5
Consumer Price Index	14.5	7.8	45.0	35.0	10.0	9.0
Current account balance, % of GDP	- 13.0	- 15.5	-17.0	-13.0	-5.0	0.0